

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA
ROOM 211
FEDERAL BUILDING AND U.S. POST OFFICE
225 SOUTH PIERRE STREET
PIERRE, SOUTH DAKOTA 57501-2463

IRVIN N. HOYT
BANKRUPTCY JUDGE

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June 2, 2005

Dennis C. Whetzal
Chapter 7 Trustee
P.O. Box 8285
Rapid City, South Dakota 57709

Bruce J. Gering
Assistant United States Trustee
230 South Phillips Avenue
Suite 502
Sioux Falls, South Dakota 57104-6321

Subject: ***In re Sturgis Meat Service, Inc.***
Chapter 7; Bankr. No. 02-50012

Dear Counsel:

The matter before the Court is Chapter 7 Trustee Dennis C. Whetzal's Amended Final Report, Proposed Distribution, and Application for Compensation ("amended final report") and the United States Trustee's objection thereto. This is a core proceeding under 28 U.S.C. § 157(b)(2)(A). This letter decision and accompanying order and judgment shall constitute the Court's findings and conclusions under Fed.Rs.Bankr.P. 7052 and 9014. As set forth below, the United States Trustee's objection will be sustained.¹

Summary. In his amended final report, which was filed on April 26, 2005, Trustee Whetzal reported total receipts of \$64,514.04. The majority of those receipts (\$45,916.36) derived from a sales tax refund from the South Dakota Department of Revenue that resulted from Debtor's erroneously paying the State sales tax on certain "Service Contracts."

Trustee Whetzal proposed, *inter alia*, to distribute

¹ The relevant facts are not in dispute. The issue presented is purely a question of law. Thus, no hearing was held.

Re: *Sturgis Meat Service, Inc.*
June 2, 2005
Page 2

\$37,392.17 to "unsecured creditors who timely filed proofs of claim on Service Contracts," whose claims total \$617,604.00. He proposed to distribute \$8,208.64 to other "unsecured creditors who timely filed proofs of claim," whose claims total \$1,427,179.44.²

The United States Trustee filed an objection to Trustee Whetzal's amended final report on May 19, 2005. In his objection, the United States Trustee stated that he did "not believe that the Bankruptcy Code allows for the special treatment of the investment contract purchasers, and that, if the sales tax refund is an estate asset, it should be distributed to all unsecured creditors pro rata."

Discussion. Pursuant to 11 U.S.C. § 726(a), "property of the estate shall be distributed . . . second, in payment of any allowed secured claim" that is either timely filed or tardily filed if the creditor did not receive timely notice of the case. Pursuant to 11 U.S.C. § 726(b), the trustee's distribution to unsecured creditors "shall be made pro rata."

In this case, there appears to be no dispute that the sales tax refund is property of the estate. In his April 26, 2005 letter, which he offered in support of his amended final report, Trustee Whetzal stated:

It is my position that the sales tax refund proceeds are property of the estate. The South Dakota Supreme Court held in *Van Emmerik v. State of South Dakota*, 298 N.W.2d 804 (S.D. 1980), that the retailer is liable for payment of sales tax, not the ultimate consumer, and that refunds may be claimed only by the "person" who made the erroneous payment. *Id.* at 806. [The South Dakota Department of Revenue] advises me that the Department has implemented the principles contained in *Van Emmerik* and confirms that it is [its] position that only the Debtor, through me in my capacity as Chapter 7 Trustee in this case, could apply for a sales tax refund from the State of South Dakota. Also, [it] asserts that it is the Debtor, not

² Trustee Whetzal proposed to make no distribution to "unsecured creditors who untimely filed proofs of claim on Service Contracts," whose claims total \$55,000.00, or other "unsecured creditors who untimely filed proofs of claim," whose claims total \$78,359.29.

Re: *Sturgis Meat Service, Inc.*
June 2, 2005
Page 3

the "consumer," i.e., the service contract holders, that was liable for the payment of sales tax in this case.

[Emphasis in original.] In his March 22, 2005 letter to Trustee Whetzal, which Trustee Whetzal offered in further support of his amended final report, Jack C. Magee, Chief Legal Counsel for the South Dakota Department of Revenue, stated:

[T]he sales tax is imposed on the retailer of tangible personal property. SDCL 10-45-2. However, the retailer has the ability to pass the tax on to the buyer. SDCL 10-45-22. If the sales tax is erroneously passed on to the buyer and then paid to the state, only the retailer, subject to some procedural restrictions (SDCL ch. 10-59), may request a refund. Van Emmerick v. State (*sic*), 298 NW2d 804, 805 (SD 1980); SDCL 10-59-17, et. seq.

There likewise appears to be no dispute that the "unsecured creditors who timely filed proofs of claim on Service Contracts" are just that, unsecured creditors. In his April 26, 2005 letter, Trustee Whetzal stated:

[I]t appears to me that the proposed treatment of service contract holders' claims as general unsecured claims in the bankruptcy is appropriate.

In his March 25, 2005 letter to Trustee Whetzal, which Trustee Whetzal offered in further support of his amended final report, Wesley W. Buckmaster, who represents many of the affected Service Contract holders, stated:

The rancher producers are creditors and not equity security holders of Sturgis Meat Service, Inc. . . . Clearly, the ranchers/cattle producers who purchased Service Contracts are general creditors in bankruptcy rather than equity holders.

The Court made Trustee Whetzal aware of its concerns regarding his proposed disparate treatment of the two "sub-classes" of timely filed unsecured claims in its March 10, 2005 letter to him and Assistant United States Trustee Gering regarding his original Trustee's Final Report, Proposed

Re: *Sturgis Meat Service, Inc.*
June 2, 2005
Page 4

Distribution, and Applications for Compensation.³ While his amended final report has answered many of the questions the Court raised in its March 10, 2005 letter, Trustee Whetzal has not pointed the Court to any authority under 11 U.S.C. § 726 that would permit him, in making his distribution, to distinguish between those unsecured creditors whose timely filed claims arose out of service contracts with Debtor and those unsecured creditors whose timely filed claims arose out of other dealings with Debtor.

Absent such authority, any distribution to unsecured creditors who timely filed proofs of claim in this case, regardless of the basis of their claims, must be made on a *pro rata* basis. Accordingly, the United States Trustee's objection will be sustained.⁴

The Court will enter an appropriate order.

Sincerely,



Irvin N. Hoyt
Bankruptcy Judge

INH:sh

cc: case file (docket original; serve parties in interest)

³ Trustee Whetzal withdrew his original Final Report, Proposed Distribution, and Applications for Compensation on March 17, 2005.

⁴ On June 2, 2005, the Court received a copy of a June 1, 2005 letter from Attorney Buckmaster to Trustee Whetzal. The gist of the letter was that "part" of the sales tax that was (erroneously) paid to the South Dakota Department of Revenue was paid out of a bank account set up to receive proceeds from Debtor's sale of the service contracts. The letter is not a part of the record before the Court. However, even if it were, the fact that "part" of the payments to the Department of Revenue was paid out of a particular bank account would not alter the Court's conclusion that the sales tax refund was property of the bankruptcy estate that must be distributed in compliance with 11 U.S.C. § 726(b).